

Chapter 1

The State of Small Business

Synopsis

Nineteen ninety-five was an excellent year for the economy and for small business. The economy gained almost 3.2 million jobs and real gross domestic product increased by 2.0 percent. The unemployment rate fell from 6.1 percent in 1994 to 5.6 percent in 1995. Consumer prices remained stable, while corporate profits and employment compensation both increased.

A record 819,477 new small firms with employees opened their doors in 1995 and new incorporations hit a record high for the third straight year. More than 22.5 million business tax returns were filed. Business failures and bankruptcies dropped for the third straight year. Bankruptcies were at their lowest level since 1981.

Corporate profits increased in 1995 for the sixth straight year. Not since the recovery from the 1981–1982 recession has such a string of increases occurred. Employment compensation and proprietorship earnings also increased.

Small-business-dominated industries added jobs to the economy at a rate more than 1.6 times the national rate of increase of 1.6 percent; large-business-dominated industries added employment at a rate well below the national rate. Small businesses are concentrated in the trade and service sectors that are growing most rapidly.

Introduction

The economy continued to grow in 1995 for the fourth consecutive year.¹ Major economic indicators reflected slow, steady and sustainable economic growth (Table 1.1). Small businesses contributed to and shared in the benefits of the growing economy.

The production of goods and services, adjusted for inflation, grew by 2.0 percent in 1995, while the unemployment rate declined from 6.1 percent to 5.6 percent. The economy added 3.2 million jobs to nonfarm payrolls; compensation to employees increased by 5.3 percent. This expansion occurred without igniting inflation: the Consumer Price Index rose by 2.8 percent and long-term interest rates declined.

¹ A comprehensive discussion of the performance of the U.S. economy appears in the *Economic Report of the President: Transmitted to the Congress February 1996* (Washington, D.C.: U.S. Government Printing Office, 1996).

Table 1.1 *Selected Indicators of Economic Performance, 1994–1995*

	1994	1995	Percent Change
Gross Domestic Product (Billions of Dollars)	6,935.7	7,253.8	4.6
Gross Domestic Product (Chained 1992 Billions of Dollars)	6,608.7	6,742.9	2.0
Unemployment Rate	6.1	5.6	
Nonagricultural Payrolls (Millions of Workers)	113.4	116.6	2.8
Compensation of Employees (Billions of Dollars)	4,009.8	4,222.7	5.3
Nonfarm Proprietors' Income (Billions of Dollars)	415.9	449.3	8.0
Corporate Profits (Billions of Dollars)	529.5	586.6	10.8
Consumer Price Index	148.2	152.4	2.8
Federal Deficit (Billions of Dollars)	203.4	163.8	–19.5
Interest Rates on:			
Long-Term Treasury Bills	7.4	6.9	
91-Day Treasury Bills	4.3	5.5	
Federal Funds	4.2	5.8	
High-Grade Corporate Securities	7.97	7.59	

Source: Federal Reserve Board of Governors, "Financial and Business Statistics," *Federal Reserve Bulletin*, April 1996, annual averages as reported in various tables.

While the federal deficit was declining by 19.5 percent (\$39.6 billion), corporate profits grew by 10.8 percent and nonfarm proprietors' income—an important measure of the health of the small business sector—rose from \$415.9 billion to \$449.3 billion.

The Number of Small Businesses

The number of businesses that filed tax returns increased by 2.3 percent in 1995 and reached almost 22.6 million (Table 1.2). Over the 13-year span from 1981 to 1994, the number of businesses grew at a compound rate of 3.8 percent per year.

Table 1.2 *Nonfarm Business Tax Returns, 1981–1995 (Thousands)*

Year	Corporations (Forms 1120 and 1120S)	Partnerships (Form 1065)	Proprietorships (Schedule C)	Total	Annual Percentage Increase
1995	4,818	1,580	16,157	22,555	2.26
1994	4,667	1,558	15,831	22,056	2.22
1993	4,516	1,567	15,495	21,578	1.64
1992	4,518	1,609	15,066	21,230	2.79
1991	4,374	1,652	14,626	20,653	1.05
1990	4,320	1,751	14,149	20,439	4.78
1989	4,197	1,780	13,529	19,506	2.78
1988	4,027	1,826	13,126	18,979	3.79
1987	3,829	1,824	12,633	18,286	4.50
1986	3,577	1,807	12,115	17,499	3.18
1985	3,437	1,755	11,767	16,959	4.88
1984	3,167	1,676	11,327	16,170	6.40
1983	3,078	1,613	10,507	15,198	5.96
1982	2,913	1,553	9,877	14,343	5.38
1981	2,813	1,458	9,345	13,616	--
Average Annual Growth Rate (Percent)	3.8	0.5	4.2	3.8	

Source: U. S. Department of the Treasury, Internal Revenue Service, *Statistics of Income Bulletin* (Spring 1996), Table 21.

Of the total, about 6 million small businesses employ between one and 500 workers. About 15,000 employ more than 500 workers and the remainder have no employees.

Business Formation and Dissolution

A record 819,477 new small firms with employees opened their doors in 1995—a 1.1 percent increase over 1994 (Table 1.3).² The number of these new firms has increased fairly steadily over the last decade, reaching successive new highs in 1993, 1994, and 1995 (Chart 1.1). Over the 1982–1995 period, the total number of firms with employees increased at a rate of just under 2 percent a year, about equal to the rates of growth of the general population and the work force.

² The United States has no formal annual survey of new business formation. Three proxies are used instead: the change in the total number of tax returns filed, the count of new firms with employees, and new incorporations. Good records of the number and size of new businesses with employees are available through the reports of employment and unemployment insurance tax liabilities to state employment security agencies. Casual business activities are less likely to be included in this measure than in the tax return total. The number of firms filing these reports is reported by the U.S. Department of Labor. Larger firms often report in more than one state, so the nationwide employment security count is about 10 percent higher than the Bureau of the Census count for the same year. Data from the Census Bureau are available only after a two-year delay, while the employment security data are available on a current basis, which makes these data particularly useful.

Table 1.3 *Change in the Number of U.S. Businesses with Employees, Fiscal Years 1982–1995 (Thousands)*

Year	Firms at End of Year	Successor Firms	New Firms	Sum: New and Successor	Terminations	Net Rate of Growth (Percent)
1995	6,057	164	819	983	871	1.09
1994	5,992	137	807	944	803	2.40
1993	5,851	136	776	911	801	1.93
1992	5,741	138	737	875	819	0.95
1991	5,687	140	724	864	818	0.84
1990	5,639	146	769	915	846	1.27
1989	5,568	153	743	896	826	1.01
1988	5,513	153	755	907	752	1.71
1987	5,420	163	775	939	717	3.64
1986	5,230	175	741	916	801	1.70
1985	5,142	166	722	888	746	2.67
1984	5,009	164	691	855	687	3.54
1983	4,837	171	633	804	720	1.26
1982	4,777	185	595	781	707	1.55

Note: Successors are existing firms taken over by new or existing firms; new firms represent applications for new account numbers; terminations represent firms that either reported being out of business or reported no employment for two years. Each quarter, firms with employees are required to report their employment, payrolls, and unemployment insurance tax liabilities to state employment services. The states in turn report the number of new firms, terminations, and successors to the U.S. Department of Labor. These statistics from the Employment and Training Administration are organized into a master file that begins in third quarter, 1981. Data in this period are available from all states except Michigan, for which a 3½-year period beginning in 1985 was estimated from previous data. Current data are available six months following the end of the quarter. The count of firms includes all active unemployment insurance taxpayers, including local, state, federal, and international governmental agencies. It includes virtually all nonfarm employers, except households, railroads, and selected religious organizations. Multistate employers submit reports to each state in which they operate; therefore, the enterprise count includes some duplication, but because multistate firms are relatively few in number, the count of firms in the United States is not significantly affected. The change in the number of firms from one period to the next represents the addition of new and successor firms less the number of terminations during the period; however, because of changes in counting rules, computer procedures, and other problems, the computed changes are sometimes at variance with the reported data. In these few cases the data are edited so that they are internally consistent.

Source: Adapted by the U.S. Small Business Administration, Office of Advocacy, from data provided by the U.S. Department of Labor, Employment and Training Administration, based upon state employment security agencies' quarterly reports, 1995.

Although the net annual increase averages just 2 percent, the level of activity in business formation and closure is actually much higher. Each year about 14 percent of small firms with employees drop from the unemployment insurance rolls, while the number of new and successor firms added is equal to about 16 percent of the total.

A high rate of business formation and dissolution is characteristic of a dynamic economy. Changing tastes and preferences, new technologies, and changes in demography and geography are all accommodated by the entry and exit of firms. New small businesses answer many of the needs, entering

Chart 1.1 *New Firms with Employees, 1982–1995*



Source: U.S. Small Business Administration, Office of Advocacy, based upon U.S. Department of Labor, Employment and Training Administration.

the marketplace with new products and services, at new locations, and with new and different methods of distribution.

The formation and dissolution of businesses varies by region across the United States (Table 1.4). Region VIII (the Mountain states) showed the largest net growth in the number of firms during 1995, posting a gain of nearly 4 percent. Regions III, V, and X all exceeded the average growth rate of new firms by wide margins.

Increases in business formation are almost always accompanied by increases in firm dissolution. For example, Region IX had the highest rates of increase in both starts and terminations, and in Region V both indicators far exceeded the national averages.

Business Incorporations

Corporations represent more than 60 percent of businesses with employees and account for nearly 90 percent of the nation's sales and employment.³ The number of new business incorporations increased by 3.8 percent in 1995 to 770,206 (Table 1.5).

³ The business incorporation series of the Dun and Bradstreet Corporation measures firms that choose to incorporate in each state and operate as corporations.

Table 1.4 *Change in the Number of U.S. Businesses with Employees by Major Region, Calendar Years 1994–1995*

	Firms at End of 1995	Change from 1994 (Percent)	New and Successor Firms		Terminations	
			Number in 1995	Change from 1994 (Percent)	Number in 1995	Change from 1994 (Percent)
Total,						
United States	6,056,668	1.09	819,477	1.56	858,391	6.86
Region I	366,090	0.31	40,328	-0.41	45,318	10.46
Region II	647,838	1.46	81,726	1.41	82,480	-4.23
Region III	590,273	2.23	72,169	3.13	73,617	1.98
Region IV	1,045,611	1.92	150,807	-9.42	152,656	-9.46
Region V	1,040,612	2.30	120,286	9.61	118,332	9.64
Region VI	614,117	1.96	83,357	-1.07	86,109	2.25
Region VII	295,063	-2.55	32,533	-0.09	38,322	3.24
Region VIII	236,143	3.71	36,541	-1.74	36,793	14.90
Region IX	917,139	-1.95	150,143	13.67	178,812	39.57
Region X	303,782	1.39	51,587	-3.57	51,260	11.55

Note: Figures for “firms at end of 1995” include successor firms, not shown in this table. SBA regions are defined as follows: Region I: Connecticut, Maine, Massachusetts, New Hampshire, Rhode Island, Vermont; Region II: New Jersey, New York; Region III: Delaware, District of Columbia, Maryland, Pennsylvania, Virginia, West Virginia; Region IV: Alabama, Florida, Georgia, Kentucky, Mississippi, North Carolina, South Carolina, Tennessee; Region V: Illinois, Indiana, Michigan, Minnesota, Ohio, Wisconsin; Region VI: Arkansas, Louisiana, New Mexico, Oklahoma, Texas; Region VII: Iowa, Kansas, Missouri, Nebraska; Region VIII: Colorado, Montana, North Dakota, South Dakota, Utah, Wyoming; Region IX: Arizona, California, Hawaii, Nevada; and Region X: Alaska, Idaho, Oregon, Washington.

Source: Adapted by the U.S. Small Business Administration, Office of Advocacy, from data provided by the U.S. Department of Labor, Employment and Training Administration, based upon state employment security agencies’ quarterly reports, 1996.

Region II (New York and New Jersey) experienced the greatest increase in incorporations (Table 1.6). The rate of increase was above the national average, due almost entirely to a 22.7 percent gain in New Jersey. Region III (the Middle Atlantic states) showed a 6.8 percent increase over 1994. Region IV (the South) had the third highest rate of growth in new incorporations, at 4.1 percent over 1994.

Business Bankruptcies and Failures

Over the past three years, the levels of both failures and bankruptcies have dropped sharply from the periods of increasing failures and bankruptcies at the beginning of the decade.

Business failures, which follow a seasonal pattern, declined overall in 1995 for the third straight year (Table 1.7).⁴ Business bankruptcies also declined over the previous year for a fourth consecutive year. The number of bankruptcies was the lowest recorded in at least 12 years.

Business failures and bankruptcies display wide variation across the regions of the country. In 1995 both measures decreased markedly in some regions (Regions I and IV) while increasing in others (Regions III, VI, VII, and X) (Table 1.8).

Most firms fail in their early years. For a given cohort, about 20 percent of the remaining firms fail in each of the first and second years after startup (Chart 1.2). The rate of failure decreases year by year; by the ninth or tenth year only about 7 or 8 percent of the remaining firms fail. Fewer than half of all new firms are in operation after five years.

Business Earnings

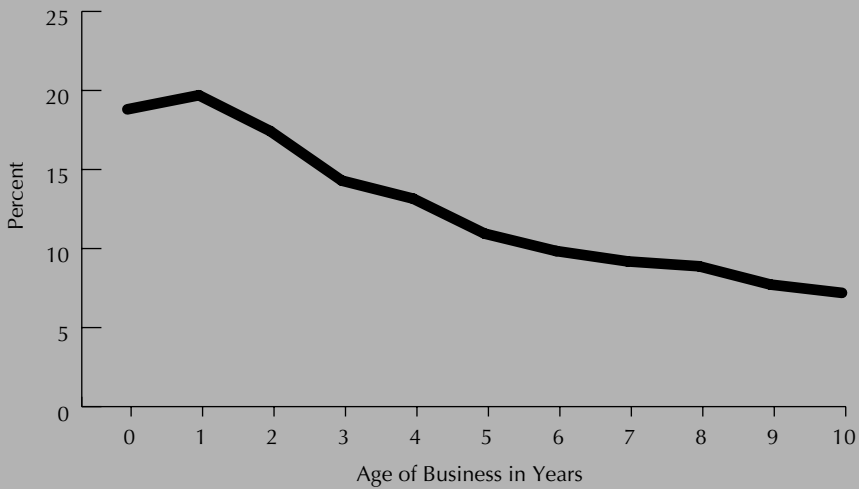
Corporate profits increased in 1995 for the sixth consecutive year (Table 1.9). Not since the recovery from the 1981 to 1982 recession has such a string of increases in corporate profits occurred. The 10.8 percent increase in corporate profits in 1995 builds upon increases of 15.7 percent in 1993 and 14.0 percent in 1994. Employment compensation increased 5.3 percent in 1995, the third largest increase since 1990.

Nonfarm proprietorship earnings, an important measure of the health of the small business sector, rose by 8.0 percent during 1995. The growth in proprietorship earnings between 1991 and 1995 was the highest for any four-year period since 1984–1988.⁵ Approximately 85 percent of small businesses are legally organized as proprietorships or partnerships.

⁴ Business failures represent business closings with a financial loss to one or more creditors that are reported to the Dun & Bradstreet Corporation. This definition is much narrower than the definition for terminations, as reported in the unemployment insurance data. Terminations represent businesses ceasing to report employment and may be closings with or without reported creditor losses. A bankruptcy is the legal recognition that a company is insolvent and not able to satisfy creditors or discharge liabilities. The company must restructure or liquidate. Not all firms, particularly those with no employees, are listed with Dun & Bradstreet and not all closing firms are reported as having an outstanding debt to a creditor. The result is that closings or “discontinuances” are about 10 times as frequent as closings with reported creditor losses. The number of bankruptcies is also about one-tenth of the overall number of business terminations. In every year observed, the number of businesses that “fail” or apply to bankruptcy court is small compared with the number that just close their doors, and is equal to about 1.5 percent of all firms reporting employment.

⁵ Nonfarm proprietorship earnings, like a number of income components other than wages and salaries, are based on Internal Revenue Service data and must be corrected for underreporting. Such corrections are difficult to make and are based on periodic IRS audit studies.

Chart 1.2 *Failure Rates by Age of Firm*



Note: Figures represent the percentage of the remaining firms that "fail"—i.e., are no longer in business at the same location—in each year after startup.

Source: U.S. Department of Commerce, Bureau of the Census, Center for Economic Studies, *The Demography of Business Failure*, Alfred R. Nucci, 1993.

Table 1.5 *New Business Incorporations, 1981–1995*

	Incorporations	Percent Change
1995	770,206	3.8
1994	741,657	5.0
1993	706,537	6.0
1992	666,800	6.1
1991	628,580	−2.9
1990	647,366	−4.3
1989	676,567	−1.2
1988	685,095	−0.1
1987	685,572	−2.4
1986	702,101	5.0
1985	668,904	5.3
1984	634,991	5.8
1983	600,400	5.9
1982	566,942	−2.5
1981	581,661	—

Source: Adapted by the U.S. Small Business Administration, Office of Advocacy, from the Dun and Bradstreet Corporation, *New Business Incorporations* (various issues).

Table 1.6 *New Business Incorporations by SBA Region, 1994 and 1995*

	1994	1995	Percent Change
U.S. Total	741,657	770,206	3.8
Region I	30,702	30,609	−0.3
Region II	101,558	110,294	8.6
Region III	103,619	110,646	6.8
Region IV	170,043	176,940	4.1
Region V	116,197	119,165	2.6
Region VI	65,278	67,199	2.9
Region VII	23,657	24,503	3.6
Region VIII	27,249	27,574	1.2
Region IX	74,934	75,497	0.8
Region X	28,417	27,779	−2.2

Note: SBA regions are defined as follows: Region I: Connecticut, Maine, Massachusetts, New Hampshire, Rhode Island, Vermont; Region II: New Jersey, New York; Region III: Delaware, District of Columbia, Maryland, Pennsylvania, Virginia, West Virginia; Region IV: Alabama, Florida, Georgia, Kentucky, Mississippi, North Carolina, South Carolina, Tennessee; Region V: Illinois, Indiana, Michigan, Minnesota, Ohio, Wisconsin; Region VI: Arkansas, Louisiana, New Mexico, Oklahoma, Texas; Region VII: Iowa, Kansas, Missouri, Nebraska; VIII: Colorado, Montana, North Dakota, South Dakota, Utah, Wyoming; Region IX: Arizona, California, Hawaii, Nevada; and Region X: Alaska, Idaho, Oregon, Washington.

Source: Adapted by the U.S. Small Business Administration, Office of Advocacy, from the Dun and Bradstreet Corporation, *New Business Incorporations* (various issues).

Small- and Large-Business-Dominated Industries

A convenient way to view the role of small business in the economy is to compare sectors dominated by small businesses with those dominated by large businesses.⁶ Some 53.1 percent of all nonfarm private sector employment in 1993 (the latest year for which data are available) was in firms with fewer than 500 employees, down slightly from 53.7 percent in 1991 (Table 1.10)

U.S. nonfarm private sector employment totaled 98.5 million in December 1995, a gain of almost 1.6 million over December 1994. The greatest gains in employment were in industries with the highest shares of employment in small firms.

⁶ Employment data by firm size are available for no later than 1992. Employment data by industry are available through 1995. The percentage employment in small firms is calculated from 1992 Census data and is used to classify industries in 1995 by employment in small or large firms. Within the major industrial sectors, the individual industries can be classified by the percentage of employment in firms with fewer than 500 employees. The classifications are as follows: small-business-dominated industries—those with more than 60 percent of employees in small firms; large-business-dominated industries—those with more than 60 percent of employees in large firms; and a remainder called “indeterminate industries”—those with between 40 and 60 percent of their employment in small or large business.

Table 1.7 *Measures of Business Failure, 1984–1995*

	Bankruptcies	Percent Change
1995	50,516	−0.6
1994	50,845	−17.7
1993	61,799	−11.5
1992	69,848	−1.1
1991	70,605	10.5
1990	63,912	2.3
1989	62,449	−0.6
1988	62,845	−22.9
1987	81,463	1.9
1986	79,926	12.2
1985	71,277	11.0
1984	64,211	2.9
	Failures	Percent Change
1995	71,194	−0.5
1994	71,558	−16.9
1993	86,133	−11.4
1992	97,069	9.9
1991	87,266	43.7
1990	60,746	20.6
1989	50,361	−11.8
1988	57,099	−6.6
1987	61,111	−0.8
1986	61,601	7.9
1985	57,067	9.6
1984	52,078	—

Sources: For failures, adapted by the U.S. Small Business Administration, Office of Advocacy, from the Dun and Bradstreet Corporation, *Business Failure Record* (various issues); for bankruptcies, from data provided by the Administrative Office of the U.S. Courts, Statistical Analysis and Reports Division.

The services industry continues to be the largest creator of new jobs, adding almost 1.1 million positions in calendar year 1995. The service sector was defined as “dominated” by small businesses (with 60 percent or more of its employment in firms with fewer than 500 employees) until 1991. Small businesses still constitute 57.6 percent of the employment in this sector.

The largest numbers of new jobs in small-firm-dominated service sectors occurred in offices of physicians and other health practitioners (119,000); engineering, accounting and research (102,000); services to buildings (26,000);

Table 1.8 *Change in Business Failures and Bankruptcies by SBA Region, 1994–1995*

	Business Failures		Percent Change 1994– 1995	Bankruptcies		Percent Change 1994– 1995
	1994	1995		1994	1995	
U.S. Total	71,558	71,194	–0.5	50,845	50,516	–0.6
Region I	3,771	3,389	–10.1	2,224	2,016	–9.4
Region II	7,730	7,842	1.4	4,765	4,569	–4.1
Region III	6,363	6,781	6.6	5,112	5,215	2.0
Region IV	9,694	8,824	–14.5	6,917	6,009	–13.1
Region V	8,504	8,340	–1.9	7,420	7,558	1.9
Region VI	8,355	9,103	9.0	5,361	5,662	5.6
Region VII	2,717	2,950	8.6	1,697	1,708	0.6
Region VIII	2,096	2,359	12.5	1,440	1,422	–1.3
Region IX	18,908	18,467	–2.3	13,451	13,691	1.8
Region X	3,420	3,679	7.6	2,458	2,666	8.5

Sources: For failures: adapted by the U.S. Small Business Administration, Office of Advocacy, from the Dun and Bradstreet Corporation, *Business Failure Record* (various issues); for bankruptcies: from data provided by the Administrative Office of the U.S. Courts, Statistical Analysis and Reports Division.

Table 1.9 *Employment Compensation, Nonfarm Proprietorship Income, and Corporate Profits, 1982–1995 (Billions of Dollars)*

Year	Employment Compensation ¹		Nonfarm Proprietorship Earnings		Pre-Tax Corporate Profits ²	
	Amount	Percent Change	Amount	Percent Change	Amount	Percent Change
1995	4,222.7	5.3	449.3	8.0	586.6	10.8
1994	4,009.6	5.3	415.9	7.2	529.5	14.0
1993	3,809.5	4.5	388.1	4.5	464.4	15.7
1992	3,644.9	5.4	371.5	11.7	401.4	4.9
1991	3,457.9	3.1	332.7	2.5	382.5	3.5
1990	3,352.8	6.4	324.6	5.3	369.5	3.7
1989	3,151.6	6.0	308.2	4.6	356.4	–0.2
1988	2,973.9	7.8	294.7	13.1	357.2	15.3
1987	2,757.7	7.2	260.6	7.4	309.7	14.3
1986	2,572.4	6.0	242.6	4.3	271.0	–4.0
1985	2,425.7	7.5	232.5	9.1	282.2	5.2
1984	2,257.0	10.4	213.1	21.2	268.2	26.3
1983	2,044.2	6.0	175.8	14.5	212.3	33.4
1982	1,927.6	153.5			159.2	

¹ Includes employee contributions for Social Security insurance.

² Includes inventory valuation and capital consumption adjustment.

Note: The data are seasonally adjusted at annual rates.

Source: U.S. Department of Commerce, Bureau of Economic Analysis, *Survey of Current Business*, Table 1.14, January 1997.

Table 1.10 *U.S. Employment by Industry, December 1994 and December 1995*

Industry	1993 Small Business Share (Percent)	December 1994 Employment (Thousands)	December 1995 Employment (Thousands)	Employment Change (Thousands)
Total, All Industries	53.1	96,858	98,481	1,623
Mining	40.9	593	569	224
Construction	88.9	5,073	5,206	133
Manufacturing	38.5	18,481	18,315	2166
Transportation, Communications and Public Utilities	35.8	6,183	6,298	115
Wholesale Trade	67.6	6,226	6,392	166
Retail Trade	53.6	21,344	21,577	233
Finance, Insurance, and Real Estate	43.9	6,915	6,987	72
Services	57.6	32,043	33,137	1,094

Source: Employment is from the U.S. Department of Labor, Bureau of Labor Statistics, *Employment and Earnings* (Washington, D.C.: U.S. Government Printing Office, March 1996), Table B-12. Employment share is calculated from special tabulations for the U.S. Small Business Administration by the U.S. Department of Commerce, Bureau of the Census, based upon 1993 measurements.

and residential care (22,000). Many of these new jobs came from births of new small firms, which are incompletely captured in the available data from the Census Bureau, and from the unincorporated self-employed, which are also omitted from Census employment counts.

It is also likely that some large firms are growing and entering industries dominated by small firms. When a large firm transfers resources to a growing sector, no net jobs may be created, but small firms' (static) employment share in that sector may decline (as in services). Examples may be found in health services, child care, and auto dealerships, where mergers and consolidation have been occurring. These dynamic changes are probably at least partially responsible for declines in small firms' measurable share of services employment. Because of incomplete data, these indicators reveal only incomplete information about small firm job creation.

Retail trade, which added 233,000 new jobs, was the next largest contributor to employment. Construction added 133,000 new jobs. More than 88 percent of employment in the construction industry was in firms with fewer than 500 employees.

Comparisons among industrial sectors illustrate the importance of small businesses in the growth of employment. Employment in smaller firms grows

Table 1.11 *Employment Change by Industry Type, December 1994 to December 1995*

Type of Industry	Total Employment Beginning of Period (Millions)	Employment Change (Thousands)	Percent Change
Small-Business-Dominated	41.9	1,072.2	2.56
Indeterminate	17.2	352.4	2.05
Large-Business-Dominated	32.6	77.4	0.24
Total	91.8	1,499.3	1.63

Note: Small firm dominance is calculated at the three-digit Standard Industrial Classification (SIC) level. Total employment at the beginning of the period was 96.9 million; the difference from the total shown reflects the omission of those industries whose employment is not reported at the three-digit SIC level.

Source: U.S. Department of Labor, Bureau of Labor Statistics, *Employment and Earnings* (February 1996), Table B-12 and Bureau of the Census, special tabulation for the U.S. Small Business Administration, Office of Advocacy, 1993. *Employment and Earnings* was used to measure employment; the special Census tabulations were used to determine small- and large-firm domination.

faster than employment in larger firms in growing industries, not necessarily because smaller firms are more efficient in their operation, but because of demand for the output of the industry and the high level of entry of smaller firms.

As employment in successful small firms increases within a growing industry and larger firms enter from other industries, the average firm size increases. The percentage of small business employment in the industry may then decline slightly, even though small businesses are supplying most of the net new jobs.⁷

The rate of employment growth in small-business-dominated industries in 1995 was higher than the national average and 10 times the employment growth in large-business-dominated industries (Table 1.11).

Employment rose by 1.5 million overall between December 1994 and December 1995; job creation varied considerably across sectors and firm sizes. Employers in large-business-dominated industries added only 77,400 jobs, while small-business dominated industries added 1.1 million (Table 1.12).

The rates of employment growth demonstrate the importance of small business in intrasector employment growth (Table 1.13). Small-business-dominated industries in transportation showed the largest percentage gain, with

⁷ Without specific data on business entries and exits, it is not possible to know the precise reasons for a declining or rising share of small firm employment in any particular sector. However, it is not inconsistent for small firms to create many or most of the new jobs in a given industry and then show a declining market share by the end of the period if large firms enter that industry. Static employment data are based on information at the end of the period, not during the period when jobs are created. The Census Bureau data received by the SBA do not measure or indicate large firm entries into industries that were formerly small-business-dominated.

Table 1.12 *Change in Employment by Size Category and Major Industry, December 1994 to December 1995 (Thousands)*

Industry	Industry Totals	Small-Business-Dominated Industries	Indeterminate Industries	Large-Business-Dominated Industries
Total, All Industries	1,502	1,072.2	352.4	77.4
Mining	-23	0.6	-5.0	-18.3
Construction	102	102.4	NA	NA
Manufacturing	-159	-3.2	-29.0	-126.4
Transportation and Utilities	117	7.2	35.8	24.2
Wholesale Trade	175	99.6	75.5	0.1
Retail Trade	272	232.5	21.0	-36.3
Finance	60	45.6	-11.9	25.9
Services	1,012	537.5	266.6	208.2

NA = Indicates lack of industry representation within that size category.

Note: Data exclude self-employed workers. Small-business-dominated industries are industries in which 60 percent or more of employment is in firms with fewer than 500 employees. Large-business-dominated industries are industries that have 60 percent or more of employment in firms with more than 500 workers. A third set of industries, in which 40.1 to 59.9 percent of employment is in firms with fewer than 500 employees, constitutes an indeterminate group, where dominance is unclear.

Source: Adapted by the U.S. Small Business Administration, Office of Advocacy, from the U.S. Department of Labor, Bureau of Labor Statistics, *Employment and Earnings* (Washington, D.C.: U.S. Government Printing Office, March 1996), Table B.12. Small- and large-business-dominated industries are calculated from special tabulations prepared for the U.S. Small Business Administration, Office of Advocacy, by the U.S. Department of Commerce, Bureau of the Census, based upon 1993 measurements.

employment growth of more than 5.68 percent. Large-business-dominated mining industries grew at rates far below the national average. The service industry posted the largest numerical gain in employment among the small-business-dominated industries, with about 537,500 new jobs.

The service sector job gains in non-small-business-dominated sectors illustrate another trend: just as manufacturing and finance firms are downsizing, companies in the service industries are “upsizing.” The sector’s 208,000 new jobs in large-business-dominated industries and 266,600 new jobs in indeterminate industries reflect services’ movement toward larger firms. Of all the large-business-dominated industries, those in the services sector recorded the largest absolute and percentage increases in employment.

Many small firms are growing into large firms, and service industries previously dominated by small firms are becoming “indeterminate.” This trend is a natural result of the growth of industries and of scale economies in purchasing, advertising, management, and finance. Franchising is a frequent method of achieving such economies.

Economies of scale are appearing in many industrial sectors as a result of improved information processing and transmittal, offering faster and addi-

Table 1.13 *Change in Employment by Size Category and Major Industry, December 1994 to December 1995 (Percent)*

Industry	Industry Totals	Small-Business-Dominated Industries	Indeterminate Industries	Large-Business-Dominated Industries
Total, All Industries	1.64	2.56	2.05	0.24
Mining	-4.51	1.90	-2.44	-6.14
Construction	2.39	2.39	NA	NA
Manufacturing	-1.21	0.08	-0.76	-1.21
Transportation	2.04	5.68	1.66	0.94
Wholesale Trade	2.61	2.50	2.97	0.05
Retail Trade	1.23	1.92	2.69	-0.49
Finance	0.91	2.09	-1.79	0.70
Services	3.44	3.75	3.75	2.62

NA = Indicates lack of industry representation within that size category.

Note: Data exclude self-employed workers. Small-business-dominated industries are industries in which 60 percent or more of employment is in firms with fewer than 500 employees. Large-business-dominated industries are industries that have 60 percent or more of employment in firms with more than 500 workers. A third set of industries, in which 40.1 to 59.9 percent of employment is in firms with fewer than 500 employees, constitutes an indeterminate group, where dominance is unclear.

Source: Adapted by the U.S. Small Business Administration, Office of Advocacy, from the U.S. Department of Labor, Bureau of Labor Statistics, *Employment and Earnings* (Washington, D.C.: U.S. Government Printing Office, March 1996), Table B.12. Small- and large-business-dominated industries are calculated from special tabulations prepared for the U.S. Small Business Administration, Office of Advocacy, by the U.S. Department of Commerce, Bureau of the Census, based upon 1993 measurements.

tional channels of distribution. The relative increases in the indeterminate classification are attributed to the growth of some previously small entities, the entry of larger firms, and the downsizing of previously large firms whose employment has fallen below 500. Industrial sectors differ as to which of these factors is most active.

Employment Changes and Firm Size

One way to look at the changing composition of employment growth in the United States is to examine the 15 small-business-dominated industries and the 15 large-business-dominated industries exhibiting the largest gains in industry employment (Table 1.14).⁸

⁸ Data on employment changes by firm size are not available on a current basis. As stated in Tables 1.12 and 1.13, the small-business-dominated concept is used instead—in which small-business-dominated industries have at least 60 percent of employment in firms with fewer than 500 employees based on 1993 Census data. Because of data limitations, it is possible for a small-firm-dominated industry to contain growing large firms, or vice versa.

Table 1.14 *Industries Generating the Most New Jobs, December 1994 to December 1995*

	Employment Change (Thousands)
Small-Business-Dominated Industries	
Eating and Drinking Places	108.1
Management and Public Relations Services	98.4
Offices and Clinics of Doctors of Medicine	53.1
Miscellaneous Amusement and Recreation Services	43.5
Plumbing, Heating, and Air Conditioning	40.3
Offices and Clinics of Other Health Practitioners	36.4
Electrical Work	34.8
Offices and Clinics of Dentists	29.2
Motor Vehicle Dealers (New and Used)	28.5
Accounting, Auditing, and Bookkeeping Services	28.2
Automotive Repair Shops	27.9
Engineering, Architectural, and Surveying Services	26.5
Local and Suburban Passenger Transportation	24.8
Real Estate Agents and Managers	22.7
Residential Care	22.0
Total, Top 15 Industries	624.4
Large-Business-Dominated Industries	
Personnel Supply Services	82.4
Grocery Stores	68.3
Hospitals	49.5
Motion Picture Production and Allied Services	47.0
Electronic Components and Accessories	45.1
Accident and Health Insurance and Medical Service Plans	21.1
Air Transportation, Scheduled, and Air Courier Services	17.4
Cable and Other Pay Television Services	17.1
Colleges, Universities, Professional Schools, and Junior Colleges	13.3
Automotive Rental and Leasing, Without Drivers	12.3
Meat Products	9.1
Personal Credit Institutions	8.3
Airports, Flying Fields, and Airport Terminal Services	7.8
Telephone Communications	7.7
Business Credit Institutions	7.3
Total, Top 15 Industries	413.7

Source: Adapted by the U.S. Small Business Administration, Office of Advocacy, from data supplied by the U.S. Department of Labor, Bureau of Labor Statistics, Employment and Training Administration. The size distribution is taken from special tabulations prepared by the U.S. Department of Commerce, Bureau of the Census, 1993.

The 15 largest job-creating industries within both the small-business-dominated and the large-business-dominated groups together added more than one million jobs. No manufacturing industries are to be found among the small-business-dominated group. Employment gains in the help supply service industry and in retail grocery stores led the gains in the large-business-dominated group. Eating and drinking places and management and public relations services, among the small-business-dominated industries, created the most new jobs.

The 15 fastest-growing small-business-dominated industries feature management and public relations services and two transportation industries (Table 1.15). Large-business-dominated industries with both high percentage and high absolute gains in employment are temporary help supply services and motion picture production.

The changing structure of industry can also be viewed through a review of the industries losing the most jobs (Table 1.16). Seven of the 15 small-business-dominated industries losing the most jobs are in manufacturing, in spite of the low small business representation in that sector overall. The employment loss percentages are small for this group, but together they account for more than half of the job losses among the top 15 losers.

The large-business-dominated industries continued to experience large job losses in the aerospace and defense industries. Department stores and family clothing stores led the list of large-business-dominated industries with the largest declines in employment.

The jobs lost among large-business-dominated industries are in very different sectors from the jobs gained by small-business-dominated industries. Moreover, the number of jobs lost in the 15 large-business-dominated sectors was 2.75 times the number of jobs lost in the 15 top small-business-dominated job losers.

Conclusion

Nineteen-ninety-five was an excellent year for the economy, for business, and for small business. The economy gained almost 3.2 million jobs and real gross domestic product increased by 2.0 percent. The unemployment rate fell from 6.1 percent in 1994 to 5.6 percent in 1995. Consumer prices were stable, as were wholesale prices. Corporate profits and employee compensation both increased.

Small-business-dominated industries added jobs to the economy at a rate more than 1.6 times the national rate of increase of 1.6 percent; large-business-dominated industries added employment at a rate well below the national rate. Small businesses are concentrated in the trade and service sectors that are growing and consolidating most rapidly. Within the trade and service sectors many small business owners view business growth as an important goal for their firms. As their businesses become larger, the small business share of employment in these sectors is declining—an indicator that small businesses are succeeding in generating economic growth.

Table 1.15 *Fastest Growing Industries, December 1994 to December 1995*

	Employment Change (Thousands)	Employment Change (Percent)
Small-Business-Dominated Industries		
Management and Public Relations Services	98.4	13.33
Local and Suburban Passenger Transportation	24.8	11.80
Arrangement of Transportation of Freight and Cargo	18.6	10.81
Taxicabs	3.4	10.30
Offices and Clinics of Other Health Practitioners	36.4	9.25
Advertising	19.6	8.51
Miscellaneous Equipment Rental and Leasing	16.6	7.56
Special Industry Machinery except Metalworking	11.7	7.29
Furniture and Home Furnishings	10.5	7.15
Mailing, Reproduction, Commercial Art and Photography, and Stenographic Services	19.0	7.07
Carpentry and Floor Work	14.9	6.88
Vocational Schools	5.3	6.80
Automotive Services except Repair	11.9	6.10
Electrical Work	34.8	5.84
Musical Instruments	0.8	5.84
Total, 15 Fastest Growing Industries	326.7	8.90
Large-Business-Dominated Industries		
Motion Picture Production and Allied Services	47.0	18.07
Cable and Other Pay Television Services	17.1	11.38
Business Credit Institutions	7.3	8.41
Electronic Components and Accessories	45.1	8.05
Intercity and Rural Bus Transportation	1.7	7.46
Airports, Flying Fields, and Airport Terminal Services	7.8	7.16
Accident and Health Insurance and Medical Service Plans	21.1	7.03
Tires and Inner Tubes	5.5	7.02
Automotive Rental and Leasing, Without Drivers	12.3	6.85
Personal Credit Institutions	8.3	5.95
Holding Offices	5.3	5.05
Personnel Supply Services	82.4	3.38
Refrigeration and Service Industry Machinery	6.4	3.28
Motion Picture Theaters	3.7	3.26
Chemical and Fertilizer Mineral Mining	0.4	2.86
Total, 15 Fastest Growing Industries	271.4	5.71

Source: Adapted by the U.S. Small Business Administration, Office of Advocacy, from data supplied by the U.S. Department of Labor, Bureau of Labor Statistics, Employment and Training Administration. The size distribution is taken from special tabulations prepared by the U.S. Department of Commerce, Bureau of the Census, 1993.

Table 1.16 *Industries Losing the Most Jobs, December 1994 to December 1995*

	Employment Change (Thousands)	Employment Change (Percent)
Small-Business-Dominated Industries		
Women's, Misses', and Juniors' Outerwear	-31.7	-11.27
Miscellaneous Fabricated Textile Products	-11.1	-5.11
Sawmills and Planing Mills	-7.6	-4.01
Labor Unions and Similar Labor Organizations	-6.8	-4.86
Farm-Product Raw Materials	-4.7	-4.15
Arrangement of Passenger Transportation	-4.6	-2.31
Girls', Children's, and Infants' Outerwear	-4.4	-9.95
General Contractors-Nonresidential Buildings	-4.2	-0.71
Household Appliance Stores	-3.4	-4.20
Millwork, Veneer, Plywood, and Structural Wood Members	-3.3	-1.20
Heavy Construction except Highway and Street	-2.9	-0.57
Miscellaneous Apparel and Accessories	-2.9	-7.32
General Contractors-Residential	-2.8	-0.46
Costume Jewelry, Costume Novelties, Buttons, and Notions		
Except Precious Metal	-2.6	-9.12
Bowling Centers	-1.4	-1.56
Total, 15 Largest Job Losers	-94.4	-2.77
Large-Business-Dominated Industries		
Department Stores	-48.4	-1.94
Family Clothing Stores	-30.7	-8.42
Men's and Boys' Furnishings, Work Clothing, etc.	-29.3	-11.04
Aircraft and Parts	-25.8	-5.54
Miscellaneous General Merchandise Stores	-16.7	-7.80
Knitting Mills	-14.2	-7.22
Search, Detection, Navigation, Guidance, Aeronautical and Nautical Systems, Instruments, and Equipment	-13.7	-8.02
Crude Petroleum and Natural Gas	-12.4	-7.92
Electric Services	-12.3	-2.99
Life Insurance	-12.3	-2.15
Guided Missiles and Space Vehicles and Parts	-9.9	-9.48
Petroleum Refining	-9.8	-8.95
Canned, Frozen, Preserved Fruits, Vegetables, and Specialties	-9.5	-4.30
Women's Clothing Stores	-7.4	-2.02
Gas Production and Distribution	-7.1	-4.50
Total, 15 Largest Job Losers	-259.5	-4.14

Source: Adapted by the U.S. Small Business Administration, Office of Advocacy, from data supplied by the U.S. Department of Labor, Bureau of Labor Statistics, Employment and Training Administration. The size distribution is taken from special tabulations prepared by the U.S. Department of Commerce, Bureau of the Census, 1993.